87-304

Supreme Court, U.S.
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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

WILLIAM LEIGHTON,

Petitioner, Objector-Appellant below,

v.

(1) BEATRICE COMPANIES, INC. et al.

(2) Kohlberg, Kravis, Roberts & Co.

and Joel B. Smilow,

(3) James L.Dutt,

Respondents, Defendants-Appellees

below.

PETITION FOR CERTIORARI TO THE SUPREME COURT OF DELAWARE

William Leighton

Petitioner

249 West 11th Street

New York, N.Y.,10014

(212)255-0001

August, 1987

Question Presented

Whether Article VI, Second Clause, of the Constitution of the United States requires the Delaware courts to apply the provisions of the Investment Company Act of 1940, the Securities Exchange Act of 1934 and the Securities Act of 1933 to the Beatrice-BCI merger, upon the objection of petitioner, a beneficial shareholder of Beatrice before the effective time of the merger, regardless of whether petitioner would have had standing, under Delaware law, to sue as a plaintiff in order to enjoin the consummation of the merger.

List of Parties

Petitioner William Leighton, objector and appellant below, became a beneficial shareholder of Beatrice before the Effective Time of the Beatrice-BCI merger by purchase of shares on the New York Stock Exchange and has since been continuously a preferred shareholder of BCI Holdings Corporation, Beatrice's successor in interest by virtue of Delaware law.

Respondent, defendant and appellee below, Beatrice Companies, Inc., is a Delaware corporation which, until April 18, 1986, was listed on the New York Stock Exchange. Beatrice had assets of about $6,200,000,000, 50,000 shareholders and was then engaged in interstate commerce as is BCI, its successor in interest under Delaware law. Over petitioner's objection, BCI has not been

made a party to this proceeding.

Respondent, defendant and appellee below, Kohlberg, Kravis, Roberts & Co., ("KKR") is a New York partnership which has created BCI for the ostensible purpose of taking over Beatrice. The real purpose was to bring about the liquidation and dissolution of Beatrice without the prior knowledge or consent of Beatrice shareholders of record and beneficial as of April 17, 1986.

The individual respondents, defendants-appellees below represented by counsel for Beatrice are : Angelo R. Arena, Bernard A. Monaghan, Omer G. Voss, Murray L. Weidenbaum, Alexander Brody, G.A. Constanzo, Walter J. Leonard, Goff Smith, James W. Cozad, Cedric E. Ritchie, William G. Karnes, Jayne B. Spain, Russell Wagner, William W. Granger, Jr., David E. Lipson, Frank E. Grzelecki,

Anthony Luiso, William S. Mowry
and Richard J. Pigott.

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Texaco Inc. v. Pennzoil,

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U.S.A. v. Carpenter et al.,

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Weiss v. Temporary Investment Fund,

465 U.S. 1001 (1984).

Official and Unofficial Reports

To date, the Chancery Court's ("Ch.") opinion of April 16, 1986, R.1a - 34a. has not been published. A final order and judgment, R. 35a - 40a, was entered on the same day.

The Delaware Supreme Court's ("DSC") order dismissing petitioner's appeal (but affirming the judgment on the appeal of another objector), R. 50a - 66a, has not been published. It is mentioned, however at 522 A.2d 865 (1987).

A petition for rehearing (which, under DSC Rule 18 is known as "motion for reargument") was denied on March 24, 1987.

Jurisdiction

The date of DSC's judgment sought to be reviewed is February 20, 1987. The

date of the order denying a motion for reargument (petition for rehearing) is March 24, 1987.

By Order of MR. JUSTICE BRENNAN dated June 19, 1987, petitioner's time to petition for certiorari was extended to and including July 22, 1987. By Order of MR. JUSTICE WHITE, petitioner's time was further extended to and includidng August 21, 1987.

Jurisdiction to review this case by writ of certiorari is conferred upon this Court by 28 U.S.C. Sec. 1257(3). As this case involves the constitutionality of Delaware statutes and rules, copies of this petition have been served upon the Attorney General of the State of Delaware, Rule 28(c).

Constitutional Provisions, Statutes, Rules and Regulations

Constitution of the United States, Article VI, Section 2 :

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the Supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

Investment Company Act of 1940, 15 U.S.C. Sec. 80a:

Sec. 3(a). When used in this title, "investment company" means any issuer which --- (3) is engaged or proposes to engage in the business of

investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40 percentum of the value of such issuer's total assets * * *

(b)Notwithstanding paragaraph (3) of subsection (a), none of the following persons is an investment company within the meaning of this title: * * * (2) any issuer which the Commission, upon application by such issuer, finds and by order declares to be primarily engaged in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities * * *.

The filing of an application under this paragraph in good faith by an issuer other than a registered investment comapny shall exempt the applicant for a period of sixty days from all provisions of this title applicable to investment companies as such. * * *

Transactions by Unregistered Investment Companies

Sec. 7(a). No investment company organized or otherwise created under the laws of the United States or of a State and having a board of directors, unless registered under section 8, shall directly or indirectly--

(1) offer for sale, sell, or deliver after sale, by the use of the mails or any means or instrumentality of interstate commerce, any security or any interest in a security whether the issuer of such security is such investment company or another person; or offer for sale, sell or deliver after sale any such security or interest, having reason to believe that such security or interest will be made the subject of a public offering by use of the mails or any means or instrumentality of interstate commerce;

(2) purchase, redeem, retire, or otherwise acquire or attempt to acquire, by use of the mails or any means or instrumentality of interstsate commerce, any security or any interest in a security, whethere the issuer of such security is such investment company or another person;

(3) control any investment company which does any of the acts enumerated in paragraphs (1 and (2);

(4) engage in any business in interstsate commerce; or

(5) control any company which is engaged in any business in interstate commerce.

Validity of Contracts

Sec.47(b)(1) A contract that is made, or whose performance involves, a violation of this title, or of any rule, regulation, or order thereunder, is unenforceable by either party (or by a

nonparty to the contract who acquired a right under the contract with knowledge of the facts by reason of which the making or performance violated or would violate any provision of this title or of any rule, regulation, or order lthereunder) unless as court finds that under the circumstances enforcement would produce a more equitable result than nonenforcement and would not be inconsistent with the purposes of this title.

(3) This subsection shall not apply (A) to the lawful portion of a contract to the extent that it may be severed from the unlawlful portion of the contract, or (B) to preclude recovery against any person for unjust enrichment."

Securities Exchange Act of 1934, 15 U.S.C. Sec. 78g:

Margin Requirements

Sec. 7(a) For the purpose of preventing the excessive use of credit for the purchase or carrying of securities, the Board of Covernors of the Federal Reserve System shall, prior to the effective date of this section and from time to time thereafter, prescribe rules and regulations with respect to the amount of credit that may be initially extended and subsequently maintained on any security (other than an exempted security).

Federal Reserve Press Release

January 10, 1986

The Federal Reserve Board has adopted an interepretation applying maargin requirements to a narrow class of debt securities that are sometimes issued to obtain credit for the purchase of

margin stock in corporate takeovers.

The interpretation deals only with certain situations involving a shell corporation used to finance the acquisition of margin stock of a target company. Such a shell has : virtually no business operations; no significant business function other than to acquire and hold the shares of the target company; and, substsantially no assets or cash flow to support the credit other than the margin stock it has acquired or intends to acquire.

The interpretation clarifies that debt securities issued by such a shell are presumed to be indirectly secured by the stock to be acquired and are thus subject to provisions of Regulation G (Securities Credit by Persons Other than Banks, Brokers or Dealers).

The presumption in the interpretation that debt securities are indirectly secured by margin stock would

not apply if there is specific evidence that lenders could in good faith rely on assets other than the margin stock as collateral, such as a guaranty by the parent of the shell corporation.

The interpretation also would not apply to other general types of transactions involving operating companies with substantial assets or cash flow, or where there is an agreed-upon merger or statutory "short-form" merger.

The Board wrote clarifying language into the final version of the interpretation to narrow its scope further and to make clear that the term "indirectly secured" will continue to apply as it has in the past.

Presently, the Board has a 50 percent margin on margin stock and convertible bonds. This means that a lender may extend credit for half the value of the stock securing the credit.

The interpretation does not apply to written contracts to extend credit entered into prior to the effective date of the interpretation, January 10, 1986.*

* *

Validity of Contracts

Section 29(b) - please see footnote (3), page 85a of the Appendix to this petition.

Delaware Corporation Law

8 Del. C. Section 327

In any derivative suit by a stockholder of a corporation, it shall be averred in the complaint that the plaintiff was a stockholder of the corporation at the time of the transaction of which he complains or that his stock thereafter devolved upon him by operation of law.

Delaware Supreme Court

Rule 8.

Only questions fairly presented to the

trial court may be presented for review; provided,however, that when the interests of justice so require, the Court may consider and determine any question not so presented.

Rule 18. Reargument.

A motion for reargument may be filed with the Clerk within 15 days after filing of the Court's opinion or order unless the time is enlarged by the Court. * * *

Statement of the Case

This is a petition for certiorari by an objector to the settlement of several stockholder class actions and derivative suits which essentially sought to prevent the Beatrice-BCI merger of April, 1986. BCI is a newly formed Delaware corporation with a capitalization of $15,000 in February, 1986. Petitioner objected below on the grounds that the merger violated several provisions of the Investment Company Act of 1940, e.g. Section 7(a) thereof, and of the Securities Exchange Act of 1934, 15 U.S.C. Sec. 78g and F.R.B. Regulations U and G thereunder, see e.g. Alaska Interstate Co. v. McMillan, 402 F.Supp. 532 (D.Del., 1975). No question of petitioner's standing to object was considered by the Chancellor at the time of the "fairness" hearing on April 14,

1987. Therefore, under the strict construction of DSC Rule 8, no such question could be decided by the DSC as a matter of first impression.

On appeal to the DSC, that court refused petitioner's request, made over a year ago, to remand for the purpose of reopening the record and receiving additional evidence, R.42a - 45a, which was accumulating in the wake of the merger.

Late in August, 1986, DSC denied respondents' motion to affirm the judgment, R.46a-47a, requesting that particular attention be given to these points in petitioner's opening brief:

Point IV, KKR's tender offer for Beatrice,

Point VI, whether BCI was an indispensable party to the suits,

Point VII Applicability of the business judgment rule and

Point VIII, concealment from the

Chancellor of KKR's request for a "no-action" letter from the S.E.C. None of these points were dealt with in DSC's order of February 20, 1987 dismissing petitioner's appeal, R. 58a - 61a, and affirming the judgment on the appeal of another objector.(The two appeals had been consolidated).

Instead, DSC concentrated its fire on petitioner's standing to object, which, as aforesaid, had not been ruled upon by the Chancellor for the reason that the respondents had not raised the point at the hearing. Again, the federal questions that had been raised by petitioner in his submissions to the Chancellor were not passed upon despite extensive briefing. No oral argument was heard. R.59a.

Meanwhile, evidence became available in the wake of the mushrooming insider trading scandal that insider trading may have occurred in the stock of

Beatrice. As the drama unfolded in New York, petitioner moved to supplement the record before a decision was handed down. This request, too, was denied, R. 48a-49a. Thus, the DSC's final decision which is before this Court for review, has ignored petitioner's pleas that reality should prevail over fiction.

In October, 1986, Ilan K. Reich who had been a partner in the New York law firm of Wachtell Lipton Rosen and Katz until July, 1986 was convicted, upon his plea of guilty, of peddling inside information for profit to others and sentenced to prison. Reich is now serving his sentence. No one has asked Reich whether he had also peddled inside information about KKR's targetting of Beatrice as a takeover candidate in the summer of 1985. In May, 1987, Reich was disbarred by order of the Appellate Division, First Department of the New

York State Supreme Court and enjoined from practicing law in any form. On Wachtell Lipton's letterhead, Reich was two steps junior to Warren K. Stern, Esq., another partner of Wachtell Lipton who had appeared before the Chancellor at the "fairness" hearing. Under New York partnership law, Wachtell Lipton are charged with knowledge of, and are liable for, Reich's acts.

Then, in February, 1987, Martin A. Siegel, KKR's agent in the scheme to accumulate Beatrice stock prior to the merger, also pleaded guilty to an information charging him with conspiracy to peddle inside information and profit therefrom. No one has asked Siegel what he had done with respect to Beatrice stock while working at Kidder Peabody, a brokerage firm. Siegel has not yet been sentenced and is believed to be "singing" before a Federal grand jury in New York.

In effect, Siegel was masterminding a conspiracy to violate S.E.C. Rule 10b-13, among others. For the S.E.C.'s current views on this rule, please see its brief in Texaco, inc. v. Pennzoil Co., excerpts from which are included in the appendix, 80a-87a. In an advertisement published in the Wall Street Journal in April, 1986, Kidder Peabody gave notice that it had "assisted in the negotiations and acted as financial advisor to KKR" in the transaction.

The pending appeal before the DSC

On March 30, 1987, petitioner notified the respondents that a petition for certiorari could be filed to seek review of the DSC's final decision in No. 156, 1986 therein. As a result, the Chancellor refused to order Beatrice to pay $3,200,000 as plaintiffs' attorneys

fees and $5,000,000 to the class.

Mindful of the requirements of this Court's Rule 21.1.(h), petitioner undertook a second round of efforts in order to persuade the Chancellor to vacate the judgment of April 16, 1986. Obviously, if that judgment had been vacated, there would have been no need to apply for certiorari.

The second round has resulted in the Chancellor's decision of June 23, 1987, R.68a - 70a. A motion for reargument was denied on July 6, R. 71a. Notice of appeal to DSC was filed on July 22, 1987, R. 73a.

Meanwhile, the time to petition for certiorari was running and this petition had to be filed.

The pending appeal in DSC will consist of a final effort in the Delaware courts to have DSC decide federal questions consistent with this Court's

decisions in such cases as Herman & MacLean v. Huddleston, 459 U.S. 375 (1983) and Transamerica Mortgage Advisors v. Lewis, 444 U.S. 11, regardless of 8 Del. C. 327.

Petitioner is aware of the basic principle that two courts cannot have jurisdiction of the same cause at the same time. In light of the Delaware courts' consistent refusal to decide federal questions and the Chancellor's holding that this petitioner has "no standing to litigate any aspect of this matter", R.70a, (a holding which the defendants could argue, in other forums, that it is res judicata), it is time that the matter should be brought to this Court's attention after a sixteen months' journey through the Delaware courts.

Petitioner's claim is based on the

Beatrice-BCI prospectus of March 11, 1986, R.74a - 79a, which governed all sales of Beatrice common stock during the period of its validity, March 11 - June 9, 1986. The prospectus has not been considered by the Chancellor despite petitioner's repeated efforts to have him look at it. The respondents have seen to it, in April, 1986, that the Chancellor should be spared the surprises that it contains.

In so doing, the respondents have acted out of their self-interest and greed. The prospectus falsely stated that Donald P. Kelly, who was therein described as a partner in Kelly, Briggs & Associates, would become a director of BCI. In effect, Mr. Kelly was to become and did become BCI's Chief Executive Officer and had a Plan for the Liquidation and Dissolution of Beatrice. Nothing in the prospectus even remotely

hinted at the existence of such a Plan, which became effective on May 29, 1986, six weeks after the "fairness" hearing before the Chancellor.

The prospectus also described the terms of the preferred stock which the Chancellor had praised as a major achievement of the settlement worth at least $130,000,000 to the class, R.19a.

Turning a closed eye to the requirements of Section 7(a) of the 1940 Act, the Chancellor did not go to the trouble of examining the legal basis for the issuance of such stock without an exemption from that provision of the Act, see Sec. 3(b)(2) thereof. The preferred no longer exists because KKR has called it in July, 1986 for exchange into debentures. In turn, $800,000,000 of the debentures were called in November, 1986 resulting in a yearly profit to KKR's partnerships of $122,000,000 for the

16-year assumed life of the debentures, or $1,952,000,000. ($800,000,000 x 15.25%=$122,000,000 x 16=$1,952,000,000). The $800,000,000 came out of the liquidation of Beatrice's assets.

On the pending appeal, the DSC may or may not reverse the Chancellor and direct him to see that federal laws are being observed by KKR. Judging by its previous decision, it is likely, however, that DSC will again take refuge behind 8 Del. C. Sec. 327. This is a situation that should be resolved by this Court.

The upshot of this lawlessness is that KKR has been able to realize hundreds of millions of dollars from its misdeeds which the Chancellor refuses to order to have audited per this petitioner's request, R.68a - 69a. As a result result KKR has hundreds of millions of dollars at its disposal whereas this petitioner and other Beatrice shareholders have nothing. This

is hardly consistent with the principle of Equal Justice under the Law.

With nothing in their hands except their stock, the shareholders are supposed to match respondents' legal resources in the defense of their federal rights.

When and How the Federal Questions Were Raised Below

Initially, the federal questions were raised by written submissions to the Chancellor dated April 4 and 14, 1986. The Chancellor passed on these in terse terms, R.25a. Federal questions were again raised by motion for reargument. This was denied on April 25, 1986, R.41a.

At the appellate level, federal questions were set forth at length in petitioner's opening and reply briefs. Once more, they were disregarded as unimportant, R.57a, 59a.

On the second round, federal

questions were raised and the opening pages of the March 11, 1986 prospectus were again submitted to the Chancellor. Nothing came of this effort, R.68a - 70a. On July 31, 1987, the respondents moved to dismiss the second appeal (No. 231, 1987) without briefing or argument. In opposition, petitioner again raised federal questions. That motion is still pending.

Reasons for the Allowance of the Writ

1. The power to enforce Article VI, Section 2 of the Constitution rests solely and exclusively in this Court. The Delaware judges' manifest disregard for their duties under Article VI requires the intervention of this Court.

It is not the purpose of this petition to urge this Court to decide, in the first instance, the federal questions raised below.

2. In the Texaco Inc., v. Pennzoil Co. case, the Texas Court of Appeals has decided a dispositive issue under SEC rule 10b-13. While the SEC has now urged the Texas Supreme Court to reverse that ruling, R.80a - 87a, the point is that there is no jurisdictional bar to a State court's consideration of the mandates of federal law. The Delaware courts should not be permitted to create such a bar where none exists. There should be a uniform rule for State court observance of federal securities law.

3. The federal questions presented below are of great importance in the current wave of mergers and acquisitions and should be resolved first.

Forty percent of the companies listed on the New York Stock Exchange are incorporated in Delaware. This gives the

great power over interstate commerce. The Delaware courts should be specifically required to comply with the mandates of federal securities law.

4. In the recent past, this Court has twice granted certiorari to resolve questions arising under the Investment Company Act of 1940. Daily Income Fund v. Fox, 464 U.S. 523, (1984) and Weiss v. Temporsary Investment Fund, 465 U.S. 1001 (1984). The issues presented by the case at bar exceed in importance the issues decided in Daily Income Fund and Weiss.

5. At this Term, this Court will hear oral argument in U.S.A. v. Carpenter et al.No. 86-422, a relatively minor insider trading case involving a small jurisdictional amouont. The time spent by the Government on that case is wholly out of proportion to its significance.

The case at bar presents a major insider trading issue affecting 50,000

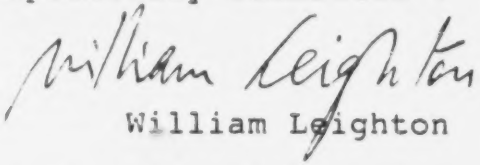
shareholders and a major corporation with $6,200,000,000 in assets. The Delaware courts have suppressed the facts with respect to insider trading on the theory that any wrongdoing, no matter how serious, is sanctioned by recourse to 8 Del. C. Sec. 327. This creates a haven for wrongdoers in Delaware and has a substantial effect on interstate commerce. The Siegel episode is illustrative of the method being used by wrongdoers. Whereas Siegel has been convicted in February, 1987 in the S.D.N.Y. for conspiracy to engage in insider trading, he has not even been summoned to appear and testify before the Chancellor concerning his relations with KKR and his trading of Beatrice stock in anticipation of KKR's tender offer.

Conclusion

The February 20, 1987 judgment of

the Delaware Supreme Court should be summarily reversed and the case remanded with directions that the Delaware courts should consider and rule on the federal questions raised by petitioner.

Respectfully submitted :



William Leighton

Petitioner, Objector-Appellant below

August, 1987